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UNITED STATES DISTRICT COURT

DISTRICT OF ARIZONA

Michael O'Connor, an Arizona resident; and Celia Rumann, an Arizona resident,

Plaintiffs,

vs.

Phoenix School of Law, LLC, a Delaware limited liability company, InfiLaw Corporation, a Delaware Corporation,

Defendants.

Case No.: 13-cv-01107-SRB

DEFENDANTS' REPLY IN SUPPORT OF MOTION TO DISMISS PURSUANT TO RULES 12(B) AND 12(B)(6)

(Assigned to the Honorable Susan Bolton)

In their First Amended Complaint, Plaintiffs, Michael O'Connor and Celia Rumann (collectively, "Plaintiffs"), claim that Defendants, Phoenix School of Law, LLC (the "School") and InfiLaw Corporation ("InfiLaw"), violated an employment contract by presenting "an 'appointment letter' rather than an employment contract in the form and style required by the Faculty Handbook." (Doc. 7, ¶ 122.) Plaintiffs allege therein that the appointment letter violated their contractual rights because the letter did not contain all necessary terms.

The School and InfiLaw have moved to dismiss Plaintiffs' breach of contract claims on grounds that, contrary to Plaintiffs' position, the appointment letter was a valid offer of employment that contained all material terms. Plaintiffs, however, rejected that valid offer and countered with a contract containing different terms. The School validly rejected that counteroffer.

In their Response, Plaintiffs appear to have abandoned the theory that the School's appointment letter was invalid because it did not contain all terms required by the Faculty

Handbook. Instead, they assert a new theory -- that the appointment letter "repudiated" their rights because it omitted certain terms that were contained in the contracts Plaintiffs signed for the prior academic year, in 2012-2013. But, the appointment letter did not omit any of the rights Plaintiffs identify. Moreover, nothing in the Faculty Handbook required the School to provide Plaintiffs with identical contract terms every year. In fact, the Faculty Handbook says just the opposite: "A tenure contract is for an academic year and gives the faculty member the contractual right to be re-employed for succeeding academic years . . . but subject to the terms and conditions of employment which exist from academic year to academic year." Plaintiffs' new theory should fare no better than their old theory.

Plaintiffs have also improperly named InfiLaw as a defendant in this breach of contract action despite that it was not Plaintiffs' employer or a party to any relevant agreement. Plaintiffs appear to argue that the Court should pierce the corporate veil and require InfiLaw to remain in the case because the School was "a mere instrumentality" of InfiLaw. Not only do the allegations contained in the First Amended Complaint not plausibly support Plaintiffs' "instrumentality" theory, but Plaintiffs do not even mention, and the First Amendment does not support, the fraud element of a veil piercing claim.

Finally, Plaintiffs' claims fail because they commenced this litigation without exhausting the School's mandatory grievance process. Plaintiffs argue that they were excused from exhaustion because the School's grievance procedures are not mandatory. Plaintiffs' position is inconsistent with binding and persuasive authority and the language of the Faculty Handbook.

I. The Appointment Letter Did Not Repudiate Plaintiffs' Contract Rights.

In May 2013, the School attempted to streamline its contract renewal process by providing its faculty with an appointment letter, which provided certain basic terms and incorporated by reference Chapter 2 of the Faculty Handbook. Plaintiffs rejected that appointment letter because "[c]ertain material terms . . . are left blank in the form contract and therefore not incorporated by the appointment letter." (Doc. 13, Exhs. E, F.)

Plaintiffs instead sent their own contracts with terms materially different than those contained in the appointment letter. Then, after the School rejected Plaintiffs' counteroffers, Plaintiffs' counsel wrote to the School, again complaining that "the Section 2.2.5 form contract omits material terms. Specifically, the dates of employment, title and rank of the faculty member, how an employee may terminate a contract, and whether the contract is subject to certain conditions are left blank." (*Id.*, Exh. F.)

Despite rejecting the School's offer of employment, Plaintiffs commenced this lawsuit. In their First Amended Complaint, Plaintiffs again complain that "[t]he form of contract that is contained in Chapter II of the Faculty Handbook contained blanks where material terms are require to be executed by the parties." (*Id.* ¶ 95.) Plaintiffs allege that "material terms of their employment -- dates of employment, title and rank, whether the contract is subject to conditions, for example -- would not have been settled because those are some of the blank terms in the form of contract appearing at Section 2.2.5." (*Id.* ¶ 98.) Nowhere in their correspondence with the School or their First Amended Complaint did Plaintiffs assert a breach of contract because the appointment letter differed from the contract they signed in 2012-2013.

The School and InfiLaw established in their Motion to Dismiss that the appointment letter and Chapter 2 of the Faculty Handbook included all material terms, including those regarding Plaintiffs' dates of employment, title and rank, and how an employee may terminate a contract.[1] Plaintiffs do not appear to argue otherwise.

Instead, Plaintiffs now claim that the School "repudiated" their contractual rights by providing them with 2013-2014 contracts containing terms that were different than their 2012-2013 contracts. Like Plaintiffs' "omitted terms" theory, this new theory fails on several fronts.

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[1] Admittedly, Plaintiffs still appear to cling to the fact that the School's form contract left the special conditions field blank while their proposed contract contained the word "none." There is absolutely no difference between the two and one would hope that Plaintiffs have not pressed a federal lawsuit against the School and InfiLaw (along with complaints to the Equal Employment Opportunity Commission and the National Labor Relations Board) because of that immaterial difference.

First, even assuming that Plaintiffs are correct that the appointment letter offered less protections than Plaintiffs' 2012-2013 contract, the appointment letter was not a "repudiation" of the parties' existing contract rights.[2] A party repudiates a contract "when he or she provides a 'positive and unequivocal manifestation' that the party will not perform when his or her duty to perform arises." *Ratliff v. Hardison*, 219 Ariz. 441, 444, 199 P.3d 696, 699 (App. 2008). "[A] mere offer to perform on terms other than those contained in the agreement, at least if the offer is made in good faith," is not a repudiation. *United Cal. Bank v. Prudential Ins. Co. of Am.*, 140 Ariz. 238, 279, 681 P.2d 390, 431 (App. 1983). The School hardly provided a "positive and unequivocal" manifestation that it would not perform. To the contrary, the School offered Plaintiffs a tenured position for a full academic year, along with a six-figure salary and all of the other rights and benefits contained in Chapter 2 of the Faculty Handbook. Even assuming that Chapter 2 contained rights and benefits slightly different from Plaintiffs' 2012-2013 contract, the School's appointment letter was no repudiation.[3]

Second, the Faculty Handbook does not require that the School provide contracts to tenured members of the faculty that are identical to those provided the year prior. The Faculty Handbook actually contemplates that contract terms may vary from year to year.[4] The Faculty Handbook states that tenure status "does not exist apart from a legally subsisting contractual agreement." (Doc. 13, Exh. A, § 2.2.4.) More importantly, the Faculty Handbook explains that tenure contracts are "subject to the terms and conditions of employment which exist from academic year to academic year."[5] (*Id.*) The School's

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[2] Plaintiffs claim that the School's cover letter admitted that the appointment letter is not a contract. What the appointment letter actually says is that it is being sent "rather than lengthy contracts." That explanation is far from an admission that the appointment letter is not a contract. In fact, the appointment letter expressly states that it constitutes an "agreement between you and Phoenix School of Law." (*See* Doc. 13, Exhs. C &D.)

[3] Plaintiffs' arguments are internally inconsistent. First, Plaintiffs argued that the School breached the Faculty Handbook because the appointment letter was not identical to the form contract contained in the Faculty Handbook. Now, they argue that the appointment letter breached the Faculty Handbook because it did not contain terms in addition to those in the Faculty Handbook. Plaintiffs cannot have it both ways.

[4] If one were to accept Plaintiffs' position, the School would be forever barred from altering the initial terms of tenured faculty members' contracts without committing a breach of contract.

[5] *Demasse v. ITT*, 194 Ariz. 500, 509-510, 984 P.2d 1138, 1147-48 (1999) is inapposite. The

appointment letter provided Plaintiffs with the terms and conditions of employment for the 2013-2014 academic year. As explained in the Motion to Dismiss, those terms and conditions were fully consonant with the Faculty Handbook.[6]

Third, contrary to Plaintiffs' position (at Doc. 15 p.6), the appointment letter did not repudiate Plaintiffs' contractual rights or provide them with less protections.

Tenure Contract. Plaintiffs complain that the appointment letter did not offer Plaintiffs a "tenure contract." The appointment letter made clear, however, that Plaintiffs were being offered a "tenure position." Other than semantics, there is no practical difference between a "tenure contract" and a "tenure position," and plaintiffs do not even attempt to explain how offering a "tenure position" was a repudiation of their rights.

Procedures Applicable Only to the School's Non-Faculty Staff. Plaintiffs argue that the appointment letter repudiated their rights because it incorporated all of Chapter 2 of the Faculty Handbook, which contains procedures not applicable to tenured faculty. Like the appointment letter, Plaintiffs' 2012-2013 contract also provided that "[t]he Contract and Employee's employment with the School are subject also to the provisions of Chapter II of the Faculty Handbook." (*See* Doc. 15, Exh. A.) Thus, Plaintiffs' 2012-2013 contract also "incorporated policies and procedures applicable only to Defendants' non-faculty staff." In this respect, therefore, the appointment letter was no different from Plaintiffs' prior contract, and it was certainly not a repudiation of their rights.

Contract Term. Plaintiffs complain that the term of their 2012-2013 contracts ran from August 1 to May 1 while the term of the 2013-2014 contracts would have run from August 19 through May 19. Although Plaintiffs are correct that the 2013-2014 term

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appointment letter was not a unilateral modification of Plaintiffs' 2012-2013 contract. It was an offer of an employment for 2013-2014, and to the extent that the appointment letter contained lesser protections than the 2012-2013 contract (which it did not), the consideration for those changes was Plaintiffs' employment, along with their six-figure salary and benefits, for the 2013-2014 academic year.

[6] The documents needed to verify that the appointment letter did not run afoul of the Faculty Handbook are each incorporated by reference in the First Amended Complaint. Plaintiffs do not dispute that the Court may refer to each of the documents attached to Defendants' Motion to Dismiss in rendering its decision.

would have started eighteen days later than the 2012-2013 term had begun, it also would have ended eighteen days later than the 2012-2013 term had ended. Thus, the 2012-2013 term was 273 days long and the 2013-2014 term would have been 273 days long. The difference in the contracts terms was, therefore, superficial at best.

Tenure Review Timeframe. Plaintiffs claim that the appointment letter "did not identify a tenure review timeframe." Plaintiffs' 2012-2013 contract stated that "the Dean and Faculty Development Committee will conduct an extensive review of each tenured faculty member every four (4) years." (*See* Doc. 15, Exh. A.) The appointment letter incorporated Chapter 2 of the Faculty Handbook, which provides that "the Dean and Faculty Development Committee will conduct an extensive review of each tenured faculty member every four (4) years." (*See* Doc. 13, Exh. A, § 2.5.6.) Thus, Plaintiffs are incorrect in alleging that the appointment letter did not identify a tenure review timeframe; the appointment letter identified the same timeframe identified in Plaintiffs' 2012-2013 contract and the Faculty Handbook.

Notice Required to Terminate. Lastly, Plaintiffs assert that the appointment letter provides less protections because it requires 90 days notice from Plaintiffs to terminate and the 2012-2013 contract required 120 days. As Defendants alluded to in their Motion to Dismiss, this change was actually beneficial to Plaintiffs. (*See* Doc. 13, p. 15 n.9.) Pursuant to the appointment letter, Plaintiffs would have had greater flexibility to terminate the contract in that they would have had to give 30 days less notice than required under their 2012-2013 contracts.

In sum, the Faculty Handbook expressly contemplates that the terms of Plaintiffs' contracts would vary from year to year. Nonetheless, not only did the appointment letter contain all material terms, but those terms also did not provide Plaintiffs with less protections than their prior contracts. Plaintiffs chose, however, to reject the School's valid employment offer and make a counteroffer, which the School was in no way required to accept. Plaintiffs' choice should not subject the School and InfiLaw to liability for breach of contract or breach of the implied covenant of good faith and fair

dealing. *See Foster v. Ohio State Univ.*, 534 N.E.2d 1220, 1222 (Ohio App. 1987).

II. Plaintiffs Cannot Pierce the Corporate Veil.

Plaintiffs have named InfiLaw as a defendant. InfiLaw, however, is not, and was not, a party to any agreements at issue in this lawsuit. Plaintiffs do not claim otherwise.

Plaintiffs now clarify that InfiLaw is a proper party to this action under a corporate veil piercing theory because the School is "a mere instrumentality of InfiLaw." (Doc. 15 at 9.) Plaintiffs' First Amended Complaint does not contain allegations plausibly supporting that the School is an instrumentality of InfiLaw. For support, Plaintiffs cite to paragraph 24 of the First Amended Complaint, which merely alleges that InfiLaw prepared the Faculty Handbook. Even assuming that allegation is true, the Faculty Handbook supports that the School is not InfiLaw's instrumentality. The Faculty Handbook indicates on its front cover that the Handbook was approved by the School's faculty, and the Handbook makes clear that it "reflects the faculty-related policies of the Phoenix School of Law, LLC." (Doc. 13, Exh. A pp. 1,7.) The Faculty Handbook also explains that the School is governed by its own independent Board of Directors, which "exercises all of the powers, rights and privileges appertaining to the company under the laws of the State of Delaware and the United States." (*Id.*, Exh. A, § 1.4.2.) The Board of Directors formulates "the general, educational, and financial policies," which are then carried out by the School's administration and faculty. (*Id.*) The School also had, at all relevant times, a Board of Advisors that made recommendations to the Board of Directors "on academic policy, standards, and processes." (*Id.* § 1.4.2.2.)

Plaintiffs also cite to paragraphs 87 and 89 of the First Amended Complaint. Those paragraphs merely allege that Plaintiffs had contracts with "Defendants" in the form of tenure contracts and the Faculty Handbook. Even a cursory review of those documents reveals Plaintiffs' allegations to be false -- only the School is a party to those contracts. (*See* Doc. 13, Exh. A; Doc. 15, Exh. A.)

Finally, Plaintiffs rely upon some discussion in the Faculty Handbook about the support and administrative services provided by an InfiLaw entity. The portions of the

Faculty Handbook that Plaintiffs rely upon do not reference InfiLaw Corporation, the defendant in this lawsuit. (*See* Doc. 13, Exh. A § 1.4.1.) Regardless, simply providing support and administrative services is insufficient to hold one of the School's owners liable for the School's alleged breach of contract.

Even assuming Plaintiffs have included sufficient allegations that the School is the mere instrumentality of InfiLaw, they have not included sufficient allegations to meet another essential element of a corporate veil piercing claim, namely that recognizing the corporate form would sanction a fraud or injustice. "[A]n alter ego theory requires not only a showing of unity of control but also proof that observance of the corporate form would sanction a fraud or promote injustice." *Horizon Res. Bethany Ltd. v. Cutco Indus.*, 180 Ariz. 72, 75, 881 P.2d 1177, 1180 (App. 1994). As noted in Fletcher Cyclopedia of the Law of Private Corporations:

> [C]ourts usually apply more stringent standards to piercing the corporate veil in a contract case than they do in tort cases. . . . [O]ne who has contracted with a selected party and received the promise bargained for should not be allowed to look to another merely because he or she is disappointed in the selected party's performance. Thus, under contract law, the disappointed one may not hold the other liable without additional compelling facts. Generally, courts find these "additional compelling facts" in affiliated corporation cases where the plaintiff has acted to his or her own detriment upon representations made by officers of the parent corporation concerning control and ownership of the subsidiary and the payment of its debts.

1 William M. Fletcher, Fletcher Cyclopedia of the Law of Private Corporations § 41.85.

Here, Plaintiffs have not alleged, and cannot allege, that observance of the School's corporate form would sanction a fraud or injustice. They also do not allege with specificity that the officers of InfiLaw made fraudulent statements to Plaintiffs regarding control and ownership of the School or payment of the School's debt. Finally, Plaintiffs do not plausibly allege that they relied on any such statement to their detriment. InfiLaw should, therefore, be dismissed from this action. *See SE Tex. Inns, Inc. v. Prime Hospitality Corp.*, 462 F.3d 666, 679 (6th Cir. 2006) (affirming dismissal of corporate defendant because the "conclusory allegations, couched in terms of a contractual breach, [were] not tantamount to the fraud or injustice required to pierce the corporate veil").

III. Plaintiffs Were Required to Exhaust the School's Grievance Procedures.

The Faculty Handbook contains detailed grievance procedures, which Plaintiffs were required to exhaust prior to commencing this lawsuit. Not only does the case law from Arizona and other jurisdictions support such a requirement, but the requirement is good policy. (*See* Doc. 13 at 10-12 (citing cases and discussing policy).)

Plaintiffs claim that they were not required to exhaust the Faculty Handbook's grievance procedures because those procedures are permissive. Plaintiffs principally rely upon *Demasse v. ITT*, 194 Ariz. 500, 515, 428 P.2d 1138, 1153 (1999), but that case is distinguishable. The grievance procedure at issue in *Demasse* required employees to discuss any problems with their supervisor. *Id.* at 514-15, 428 P.2d at 1152-53. The Court rejected the employer's exhaustion argument because "once terminated, an employee no longer has a supervisor. Thus the designated complaint avenue is cut off." *Id.* at 515, 984 P.2d at 1153. Here, Plaintiffs were required to bring their grievance to the attention of the Dean, who would have then been required to investigate the matter and respond in writing. (*See* Doc. 13, Exh. A, § 2.16.6.1 pp. 104-05.) Unlike in *Demasse*, Plaintiffs' designated complaint avenue to the Dean was not cut off once Plaintiffs rejected the School's employment offer.

Moreover, unlike in *Demasse*, the requirement that Plaintiffs submit a formal grievance to the Dean was not couched in permissive terms. In Plaintiffs' case, because the Dean was their direct supervisor, the Faculty Handbook makes mandatory that their grievances be presented to the Dean in writing:

> [T]he grievant shall formalize the grievance and file it with the Dean . . . . The formalized grievance shall be presented in writing. The written submission shall state the specific policy, regulation, or procedure alleged to have been misinterpreted, misapplied, or violated, the effect on the grievant, and the relief requested.

(*Id.*, Exh. A, § 2.16.6.2.) This is a far cry from the permissive provisions at issue in *Demasse*.

This case is more akin to this Court's decision in *Moses v. Phelps Dodge Corp.*, 818 F. Supp. 1287 (D. Ariz. 1993), where the grievance procedures were held mandatory.

The employee handbook in that case stated that the grievance procedures "*constitute the sole and exclusive procedure* for the processing and resolution of any controversy, complaint, misunderstanding or dispute that may arise concerning any aspect of your employment or termination from employment." *Id.* at 1290-91. The Faculty Handbook in this case states that "[t]hese procedures shall be the method for resolving all grievances." (Doc. 13, Exh. A, § 2.16.1 (emphasis added).) This case is, therefore, governed by *Moses*, not *Demasse*.[7]

In a last ditch effort to avoid dismissal, Plaintiffs argue that their counsel's May 10, 2013 letter constitutes a formal grievance to the Dean. That argument similarly fails. Counsel's letter was written before the School even rejected Plaintiffs' counteroffer of employment and did not indicate anywhere that it constituted a formal grievance or was intended to initiate the grievance process under the Faculty Handbook. The Court should not accept Plaintiffs' *post hoc* claim that they exhausted their remedies, and should dismiss Plaintiffs' complaint for failure to exhaust.

IV. Conclusion.

For the foregoing reasons, and those contained in Defendants' Motion to Dismiss, Defendants respectfully request that the Court dismiss Plaintiffs' First Amended Complaint with prejudice. Defendants further request that the Court award Defendants their attorneys' fees and costs as the prevailing parties in this action arising out of contract.

RESPECTFULLY SUBMITTED this 9th day of August, 2013.

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By *s/ Michael S. Catlett*
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[7] Admittedly, the Faculty Handbook does not contain the adjectives "sole and exclusive" when referring to the grievance procedures. Plaintiffs cite to no case, however, holding that those adjectives, and only those adjectives, must be used in order to make a grievance procedure mandatory.

CERTIFICATE OF FILING/MAILING

I hereby certify that on August 9, 2013, I electronically transmitted the attached document to the Clerk's Office using the CM/ECF System for filing and transmittal of a Notice of Electronic Filing to all counsel identified on the Court-Generated Notice of Electronic Filing.

s/ Frances Fulwiler